IN THE

Supreme Court of the United States

OCTOBER TERM, 1953.

No. .....

IN THE MATTER OF
THE GILL-OWEN COMPANY,
Bankrupt.

THE HILLSBORO NATIONAL BANK,
Petitioner,

vs.

J. PAUL BUSCHER, TRUSTEE IN BANKRUPTCY OF THE ESTATE OF THE GILL-OWEN CO., A BANKRUPT,
Respondent.

APPELLANT'S BRIEF.

STATEMENT.

The statement heretofore made in the Petition for review by Writ of Certiorari is hereby adopted as the statement of the case pages 2 to 15 and made a part of this brief. We are, however, stating a few additional facts.

The court of appeals in its consideration of the case has overlooked the fact that the claim for reclamation was based on two promissory notes JJ2 for the sum of $17,900.00 and JJ3 for the sum of $14,000.00, totaling $31,900.00, now claimed in the petition for reclamation (R.

86). The court has also overlooked the fact that Mr. Fisher, the president of petitioner bank testified that he had always retained the said notes JJ2 and JJ3 and had refused to surrender them to anyone because they were signed not only by the partnership, but by Gill and Owen, individually, and that he did not want to surrender the obligations of the partnership and thereby release the sureties from the payment of the same (R. 83). No one has denied this statement.

There is another question which the court of appeals has mention but it is not stated accurately. It is said in the opinion that "the record does, however, show positively that the Hillsboro National Bank did at or about the time of this transaction have actual knowledge of the transfer of the goods and chattels involved by the partnership to the corporate bankrupt." The fact about this question is that Mr. Fisher, the president of petitioner bank testified that he received notice of the transfer one or two days after it had been made (R. 70). That fixed the date as September 1st or 2nd. Gill first testified that he had several conversations with Fisher about the matter (R. 99), but he finally changed his testimony about that and reduced the conversations down to one. He first thought that it was before the transfer on August 31, 1948, but he was given some memorandum to refresh his recollection and after examination of the memorandum, he testified that the first time he ever talked to Fisher about the matter was September 1, 1948, (R. 100), so that his testimony substantially corroborates Fisher's. Owen, the other partner who owned a 60% interest in both the partnership and the corporation, testified that Fisher was furnished the information about the transfer at a much later date than that (R. 31). No other witness testified concerning this question. The record, therefore, definitely shows that petitioner did not obtain any advance information that the sale or transfer of said assets

was to be made. He was not present and did not participate in the making of such transfer, and since petitioner gained such information at least a day after the transfer had been made, and after the provisions of the Bulk Sales Act of the State of Illinois had been violated by failure to give notice to petitioner and the other creditors, there was nothing petitioner could do to set aside what had already been done.

SPECIFICATION OF ERRORS.

1. The court erred in not following the decisions of the highest court of the State of Illinois in determining the effect of the acceptance of payments received by petitioner from the corporation as constituting an estoppel.

2. The court erred in following the decision of the trial court based on no decisions of the Supreme Court of Illinois.

3. The court erred in following a rule of law announced in a headnote in 15 A. L. R. (2d) 937, which announces rules of law inconsistent with the settled law of the State of Illinois.

4. The court erred in recognizing estoppel, equitable estoppel, or quasi estoppel relative to matters as well known to the corporation as to petitioner.

5. The court erred in applying the doctrine of estoppel, equitable estoppel, or quasi estoppel against petitioner for accepting payments that were unquestionably due and owing by both the corporation and the partnership.

6. The Referee made a finding of facts in favor of petitioner; and found that neither waiver, laches or estoppel were a defense to the petition; and, the district court erred in deciding this case against petitioner, without making any finding of facts contrary to the findings of the Referee.

APPELLANT'S BRIEF.

I.

Under the Allegations and Proof, Petitioner Was Entitled to Recover Upon Its Petition for Reclamation.

Weskalnies v. *Hesterman*, 288 Ill. 199.
In re Le Maire Cosmetic Co., Inc., 174 Fed. (2d) 749.

The purpose of the Bulk Sales Act is to constitute the goods of the debtor a trust fund for the benefit of all his creditors and the purchaser is liable to the creditors to the extent of the value of the purchased property.

24 Am. Jur. 354, Sec. 244, Fraudulent Conveyances.
Corrigan v. *Miller*, 338 Ill. App. 212, 86 N. E. (2d) 853.

A purchaser in violation of the Bulk Sales Act acquired no rights in the property purchased as against the creditors of the seller. His status is that of trustee, or receiver for the benefit of all of the creditors of the seller. As such he is responsible for the disposition of the property.

27 C. J. 885, Sec. 892, Fraudulent Conveyances.

A trustee (in bankruptcy) does not acquire title to property held by the bankrupt as a mere bailee or as an agent of another neither does he acquire title to property the legal title to which is in the bankrupt as trustee.

7 C. J. 128, Sec. 218, Bankruptcy.

The trustee in bankruptcy does not acquire title to the property the legal title to which is in the bankrupt as trustee; the trustee in bankruptcy is not entitled to property in

possession of the bankrupt which is held under an implied trust, or to which a constructive trust attaches.

8 C. J. S. 650-653, Sec. 193, Sub-division "d", Bankruptcy.

Am. Service Co. v. *Henderson,* 120 Fed. 525, 135 A. L. R. 1414 at page 1420, with a note appended.

In the Matter of Rainbo Gardens, Inc., 52 Am. Bk. (N. S.) 616.

24 Am. Jur. 354, Sec. 244, Fraudulent Conveyances, *supra.*

6 Am. Jur. 1081, Sec. 897, Bankruptcy.

City of Dallas v. *Griffin,* 171 Fed. 526.

Todd v. *Petit,* 105 Fed. 139.

II.

A. The Circuit Court of Appeals Has Erroneously Applied the Doctrine of Estoppel to Defeat Petitioner in Its Right to Recover.

Walker v. *Wood,* 170 Ill. 463.

Burnett v. *West Madison State Bank,* 375 Ill. 402.

Hayward v. *Burke,* 151 Ill. 121.

Northwestern Mutual Life Ins. Co. v. *Eddleman,* 247 Ky. 116, 56 S. W. (2d) 561, 87 A. L. R. 276.

Erie R. Co. v. *Tompkins,* 304 U. S. 64, 83 L. Ed. 1188.

U. S. Supreme Court Rule 38 (5-b).

B. In Making Payments on Its Agreement and the Acceptance of Such Payments by the Petitioner, the Corporations Was Not Misled in the Least. Unless It Was Misled in Some Manner With Reference to the Facts, Neither Estoppel, Equitable Estoppel, Nor Quasi Estoppel Are Available to It as a Defense.

31 C. J. S. 349, Sec. 109 (b), Estoppel.

19 Am. Jur. 692, Sec. 65, Estoppel.

Grand Trunk etc. v. *Nelson,* 116 Fed. (2d) 22.

C. Petitioner Was Not Estopped Even By the Application of Quasi Estoppel From Receiving Said Payments on Its Debt, Because the Doctrine of Estoppel Never Applies When One Is Only Receiving That Which He Is Legally Entitled to Receive in All Events.

19 Am. Jur. 692, Sec. 65, Estoppel, *supra.*

SUMMARY OF THE ARGUMENT.

I.

Petitioner alleged and proved its case for reclamation on the theory that the partnership sold the major portion of its assets to the corporation and when neither the partnership nor the corporation had given any notice of intention to make the sale or transfer to any of the creditors of the partnership and without complying with the Bulk Sales Act of the State of Illinois, and that the sale was, therefore, void. The referee in bankruptcy found in favor of petitioner and against the trustee, respondent herein. The district court and court of appeals have both reversed the decision of the referee through the application of the doctrine of estoppel without questioning the right of petitioner to otherwise recover, and thereby impliedly recognizing the right of petitioner to recover, except for the application of the defense of estoppel, and the court of appeals erred in recognizing estoppel as a defense in this suit.

II.

A. The court of appeals has avoided the application of the Bulk Sales Act of the State of Illinois by following the decisions of courts of other states and reaching a result contrary to the rule of law established by the decisions of the highest court of Illinois which holds that the acceptance of partial payments by one who has assumed the debts of another, does not release the original obligor from its obligation to its creditor.

B. The corporation had knowledge of the fact that it had assumed and agreed to pay the debts of the partner-

ship. Making payments by the corporation on its agreement, and the acceptance of such payments by the petitioner, did not mislead it in the least. Unless it was misled in some manner with reference to the facts, neither estoppel, nor quasi estoppel are available to it as a defense.

C. Petitioner was not estopped even by the application of quasi estoppel from receiving said payments on its debt, because the doctrine of estoppel never applies when one is only receiving that which he is legally entitled to receive in all events.

ARGUMENT.

I.

Under the Allegations and Proof, Petitioner Was Entitled to Recover Upon Its Petition for Reclamation.

That the attempted sale in this case was void is well established by the holding of the Supreme Court of Illinois in the case of *Weskalnies* v. *Hesterman,* decided in 1919, and reported in 288 Ill. 199, where the facts were not far different from those involved here. The Court on page 202, there said:

> "No attempt was made by Albert Weskalnies to comply with the Bulk Sales act, and if the act applied to him, then the sale of the property to plaintiff was fraudulent and void as to creditors. The first Bulk Sales act in this State was passed by the legislature in 1905. (Laws of 1905, p. 284.) That act was expressly limited in its application to the sale of stocks of merchandise, and in *Off & Co.* v. *Morehead,* 235 Ill. 40, it was held unconstitutional. It was pointed out in that case that the act did not apply to farmers, hotel keepers, livery or transfer companies, publishers, mine owners and others mentioned, and the court held that there was no reason or qualification connected with a stock of merchandise, or persons dealing in the same, which authorized the legislature to mark it or them for special protective legislation from which all other classes of persons and property were excluded. In 1913 the legislature passed another Bulk Sales act. (Laws of 1913, p. 258.) That act declares fraudulent and void as against creditors 'the sale, transfer or assignment in bulk of the major part or the whole of a stock of merchandise, or merchandise and fixtures or other goods and chattels of the vendor's business, otherwise than in the ordinary course of trade and in

the regular and usual prosecution of the vendor's business,' without compliance with the provisions of the act. Section 3 provides that the act shall include corporations, associations, co-partnerships and individuals who are parties to any sale of goods in bulk, but not to sales by executors, administrators, receivers, trustees in bankruptcy or by any public officer under judicial process, nor to the sales of exempt property, nor to sales made in the ordinary course of trade and in the regular and usual prosecution of the vendor's business, nor to sales made in good faith at public auction when notice is published in a newspaper of general circulation in the county where the sale is made, ten days before the sale, or by posting notices in five public places ten days before the sale. That act was held valid in *Johnson Co.* v. *Beloosky,* 263 Ill. 363. The court said: 'It must be assumed that the legislature, in passing the new act, had before it the decision of this court holding the former act unconstitutional because it was special class legislation, and that it was the intention of the General Assembly in passing the later act to obviate this objection by passing a general act applicable indiscriminately to the sale of any goods and chattels in the manner inhibited by Section 1 of said act. Construing the new act as a general law which prohibits the sale of any goods and chattels in bulk, otherwise than in the ordinary course of trade in the regular and usual prosecution of business, the objection to which the former statute was open is obviated.' It seems very clear from the history of the legislation and the language of the act that it was intended to, and does, apply to the sale of the property made by Albert Weskalnies to plaintiff. It was a sale in bulk of the major portion of the vendor's property, and was not made 'in the ordinary course of trade and in the regular and usual prosecution of the vendor's business.' There was no error in the holding of the circuit and Appellate Courts that the sale was fraudulent and void as to creditors."

The United States Court of Appeals for the Seventh Circuit *In re Le Maire Cosmetic Co., Inc.,* 174 Fed. (2d) 749,

in an opinion by Major, in deciding a case involving the construction of the Bulk Sales Act of the State of Illinois, has held that sales made without giving notice to creditors, as required by Section 1 of said Bulk Sales Act of Illinois are void. The said circuit court of appeals in said case, likewise held that said Bulk Sales Act of Illinois applies to sales made between an individual and a corporation, and between a partnership and a corporation, even where the individual and the corporation, and the partnership and the corporation were all owned by the same person. The Federal Court in its said decision cites and relies upon many other Illinois cases construing the Bulk Sales Act of the State of Illinois.

The courts of some of the states have held that sales and transfers made in violation of the Bulk Sales Act of those particular states, without giving notice to the creditors of the seller is merely voidable.

The circuit court of appeals in the *City of New York* v. *Johnson,* 137 Fed. 2d 163, page 165 has held that the New York Bulk Sales Act, although very similar to the Illinois Bulk Sales Act was voidable rather than void. The circuit court of appeals *In re Le Maire Cosmetic Co., Inc.,* 174 F. (2d) 749 has squarely held that sales made in Illinois without complying with the Bulk Sales Act of Illinois are void rather than voidable. In so doing, the court of appeals in the *Le Maire* case has followed the settled law on the question as announced in *Weskalnies* v. *Hesterman, supra,* and other decisions of the Supreme Court and Appellate Court of the State of Illinois, same of which are cited in its opinion.

There has been some question raised in this case and referred to by the court in its opinion doubting whether or not the sale in question from the partnership to the corporation was governed by the provisions of the Bulk Sales Act of the State of Illinois. Some of the Bulk Sales Acts

fail to specifically provide what sellers and what purchasers are governed by the act, but Section 3 of the Bulk Sales Act of the State of Illinois (Appendix, p. 55, *infra*) specifically provides as follows:

> "Vendors and Vendees under this act shall include corporations, associations, co-partnerships and individuals, who shall be party to any sale, transfer or assignment, of goods and chattels in bulk. But nothing contained in this act shall apply to sales by executors, administrators, receivers, trustees in bankruptcy or by any public officer under judicial process nor to sales of exempt property or any sale or transfer made in the ordinary course of trade and in the regular and usual prosecution of the vendor's business nor to sales made in good faith at public auction, where notice of such sale is given in a newspaper of general circulation within the county where such sale is made, at least ten days before such sale or by posting of notices in at least five public places at least ten days before said sale."

In those states where the statutes fail to specifically state what sellers and what purchasers are controlled by the Act, it, of course, becomes a matter of construction, and the courts in construing the Bulk Sales Acts of those particular states have in some cases reached rather absurd results. In view, however, of the specific provisions of Section 3 of the Bulk Sales Act of the State of Illinois, no room for construction is left, and the Act unquestionably applies to sales made between all separate entities, and to sales or transfers from a partnership to a corporation specifically enumerated in the act. The fact that the partners of the partnership own substantially all the capital stock of the corporation can not nullify the express provisions of Section 3 of the Bulk Sales Act of the State of Illinois. *Weskalnies* v. *Hesterman, supra,* and *In re LeMaire Cosmetic Co., Inc., supra.*

The first Bulk Sales Act passed in Illinois in 1905 applied only to a sale, but after that act was declared unconstitutional, the new Act which was passed in 1913 provided that the Act applied to sales, transfers and assignments. The Bulk Sales Acts of Pennsylvania, Washington and Minnesota apply only to a sale, and not to a transfer or assignment, and it has been held in those states, properly, that if only a transfer or assignment was involved, that the Bulk Sales Act did not apply. Such was the holding in *McLean* v. *Miller, etc.*, 55 Fed. 2d 232, construing the Pennsylvania Bulk Sales Act, *Maskell* v. *Spokane*, 100 Wash. 16, construing the Washington Bulk Sales Act, and *Thorpe* v. *Pennock, Mercantile Co.*, 99 Minn. 22, construing the Minnesota Bulk Sales Act. In Illinois, the Bulk Sales Act applies to sales, transfers, or assignment, and certainly applied to the sale or transfer made by the partnership to the corporation in the case here involved.

Where an attempt has been made to sell personal property in Illinois, and the sale is void because no attempt was made to comply with the Bulk Sales Act, the purchaser holds the property so sold as a trust fund, for the benefit of the creditors of the seller.

In 24 American Jurisprudence, page 354, Section 244, Fraudulent Conveyances, it is said:

> "The purpose of the Bulk Sales Act is to constitute the goods of the debtor a trust fund for the benefit of all his creditors and the purchaser is liable to the creditors to the extent of the value of the purchased property."

See also *Corrigan* v. *Miller*, 338 Ill. App. 212, 86 N. E. 2d 853.

In 27 C. J. 885, Section 892, Fraudulent Conveyances, it is said:

> "A purchaser in violation of the Bulk Sales Act

> acquired no rights in the property purchased as against the creditors of the seller. His status is that of trustee, or receiver for the benefit of all of the creditors of the seller. As such he is responsible for the disposition of the property."

Where funds or personal property are held by the bankrupt in trust at the time he is adjudged a bankrupt, they pass to the trustee in bankruptcy in Illinois where the sale is void impressed with the same trust and they can be reclaimed from his trustee in bankruptcy.

In 7 C. J. 128, Section 218, Bankruptcy, it is said:

> "The trustee (in bankruptcy) does not acquire title to property held by the bankrupt as a mere bailee or as an agent of another neither does he acquire title to property the legal title to which is in the bankrupt as trustee."

See also 8 C. J. S., under the subject of Bankruptcy 650-653, Sec. 193, Subdivision "d", where the heading is as follows:

> "The trustee in bankruptcy does not acquire title to the property the legal title to which is in the bankrupt as trustee; the trustee in bankruptcy is not entitled to property in possession of the bankrupt which is held under an implied trust, or to which a constructive trust attaches."

The following are a few of many of the cases cited in support of the last subdivision of said Section 193, 8 C. J. S., under the subject of Bankruptcy:

Amer. Service Co. v. *Henderson,* 120 Fed. 525, 135 A. L. R. 1414, at page 1420, with a note appended.

Dallas v. *Griffin,* 171 Fed. 526 and certiorari to U. S. Supreme Ct. denied.

Todd v. *Petit,* 105 Fed. 139.

In Re Franklin Savings & Loan Co., 34 Fed. Supp. 585, aff'd 661.

In Re Gradsky v. *Site*, 30 Fed. Supp. 656 (See 8 C. J. S., Bankruptcy Section 193, also pocket supplement).

If the sale involved in this case and made by the Litchfield Precision Products to the Gill-Owen Company had been made in the State of New York rather than in the State of Illinois, then the rule applied in the *Johnson* case would apply, and the petitions for reclamation would have to be denied, but where the construction of the Bulk Sales Act is construed as making a sale had in violation of that Act void as it has in Illinois, then the trustee in bankruptcy takes only the title held by the bankrupt which was only in trust for the benefit of the creditors of the vendor and under such circumstances he holds the title in trust only for the creditors, and they are entitled to recover on their petitions for reclamation by both reasoning and authority, and as expressly held *In Re LeMaire Cosmetic Company, supra,* and in the case entitled *In the Matter of Rainbo Gardens, Inc.,* a bankruptcy, and decided by the Referee in Bankruptcy, of the Northern District of Illinois, Eastern Division, on January 11, 1943, and reported in 52 Am. Br. (NS) 616.

By the unlawful sale, the assets of the partnership passed to the corporation, in trust only, for the use and benefit of the creditors of the partnership; the acts of estoppel relied upon as a defense occurred while the corporation held the title to the property in trust for the benefit of the creditors of the partnership, and when the corporation was adjudged a voluntary bankrupt, the property, held in trust by the corporation for the use and benefit of the creditors of the partnership, passed to the respondent, the trustee in bankruptcy, in trust, for the use and benefit of the creditors of the partnership. The rights of the creditors of the bankrupt are, therefore, not involved until it is first determined

that the property in question was the property of the bankrupt. If the property in question is not the property of the bankrupt, then the rights of the creditors of the bankrupt corporation are not involved, and they are not entitled to share with the creditors of the partnership.

The purpose of the Bulk Sales Act is to constitute the goods of the debtor a trust fund for the benefit of all his creditors and the purchaser is liable to the creditors to the extent of the value of the purchased property. 24 Am. Jur. 354, Fraudulent Conveyances, Sec. 244; 6 Am. Jur. 1081, Bankruptcy, Section 897; *Corrigan* v. *Miller*, 338 Ill. App. 212, 86 N. E. 2d 853, 857.

A purchaser in violation of the Bulk Sales Act acquired no rights in the property purchased as against the creditors of the seller, his status is that of trustee, or receiver for the benefit of all of the creditors of the seller. 27 C. J. 885, Fraudulent Conveyances, Sec. 892.

The Trustee in Bankruptcy does not acquire title to the property the legal title to which is in the bankrupt as trustee; the Trustee in Bankruptcy is not entitled to a property in possession of the bankrupt which is held under an implied trust, or to which a constructive trust attaches. 8 C. J. S. 653, Bankruptcy, Sec. 193; *American Service Co.* v. *Henderson*, 120 F. 2d 525, 530; *City of Dallas* v. *Crippen*, 171 F. 2d 526, 529; *Todd* v. *Pettit*, 108 F. 2d 139, 140; *In re Franklin Savings and Loan Co.*, 34 F. Supp. 585, 586, 587; *Grodsky* v. *Sipe*, 30 F. Supp. 656, 661, 662.

The Honorable Basil H. Countrakon, Referee in Bankruptcy, who heard the testimony in this case, and after having heard the argument thereon, entered his findings as follows:

> "This cause coming on to be heard before the Honorable Basil H. Coutrakon, Referee in Bankruptcy, on the Petition of the Hillsboro National Bank for recla-

mation and the answer of the Trustee in Bankruptcy thereto, and upon the testimony of witnesses produced by the respective parties sworn and examined before the Referee, and after argument of counsel for the respective parties, the Referee finds:

1. That the Litchfield Precision Products, a partnership did, on the 28th day of August, 1948, attempt to sell its personal property to the Gill-Owen Company, a corporation, the Bankrupt herein, without complying with the provisions of the Bulk Sales Act of the State of Illinois.

2. That said attempted sale was made without any notice to any creditors of said partnership.

3. That the reclamation petitioners are not guilty of waiver, estoppel, laches or ratification.

4. That the Petitioner, The Hillsboro National Bank, as well as other creditors have filed their Petitions for Reclamation, and were, at the time of said attempted transfer, creditors of the said Litchfield Precision Products, a partnership.

5. That on the 29th day of June, 1950, an order was entered by the Referee in Bankruptcy that J. Paul Buscher, Trustee in Bankruptcy, sell all of the personal property in possession of the Gill-Owen Company, a corporation, the bankrupt, for cash, and provided that the proceeds arising from the sale thereof should be retained and kept separately by the Trustee in Bankruptcy in lieu of the property sold, and that the claims of the petitioners attach to the proceeds of such sale and stand in lieu of the property sold, and that the proceeds of the sale of said personal property be distributed under the further order of the Referee in Bankruptcy; that the highest bid made on all the personal assets offered by the Trustee was $20,800.00 and the highest bid made at said sale on the real estate was $12,000.00, but when the real and personal estate 202 were offered together they sold for $36,000.00; that 90% of the personal assets offered for sale, as aforesaid, came from the sale of the assets of Litchfield Precision Products to the Gill-Owen Company; that the Petitions for Reclamation filed on behalf of the

creditors of Litchfield Precision Products shall abide the result and decision of the Referee upon the petition of The Hillsboro National Bank for Reclamation.

6. That the Trustee in Bankruptcy on August 3, 1950, sold all the personal estate of the bankrupt, 90% of which were assets coming into his hands through the void sale of the personal assets of Litchfield Precisions Products to the Bankrupt, as aforesaid; that 90% of the total personal assets sold by the Trustee is $20,546.33; that the Trustee, therefore, has in his possession $20,546.33 cash arising from the sale of said assets which should be distributed to the petitioning creditors of Litchfield Precision Products.

7. That the said Petitioners for Reclamation are entitled to share in the proceeds of the sale of the personal property after certain costs of administration are paid in the course of administration herein as determined by this court.

It Is Therefore Ordered, Adjudged and Decreed:

1. That the attempted sale by the Litchfield Precision Products, a partnership, of its personal property on the 28th day of August, 1948, to the Gill-Owen Company, a Corporation, the Bankrupt herein, was fradulent and void as to the creditors of the said Litchfield Precision Products, being the Reclamation Petitioners herein.

2. It is further ordered, adjudged and decreed that the proceeds from the sale of the said personal property by the Trustee in Bankruptcy amounts to $20,546.33 and after certain costs of administration to be determined by this court are deducted therefrom should be distributed to the Reclamation Petitioners herein, in the course of administration herein.

Entered this 28th day of April A. D. 1952."

After the case was removed by the petition for review to the United States District Court, that court, without having heard any additional testimony, disregarding the finding of the referee, and without determining whether or not petitioner had proved its case and was entitled to recover, held

that by reason of the acceptance by petitioner of the two payments from the corporation, prior to the time it was adjudged a bankrupt, petitioner was estopped from recovering on its petition for reclamation.

The application of the doctrine of estoppel as a defense impliedly concedes, however, that petitioner would be entitled to recover except for the act claimed to effect an estoppel, and that question will be considered under the next subdivision of this argument.

II.

A. The Circuit Court of Appeals Has Erroneously Applied the Doctrine of Estoppel to Defeat Petitioner in Its Right to Recover.

The circuit court of appeals in its decision has held that petitioner is estopped from recovering under its claim. The Court in its holding has used the word estoppel ratherly loosely, because estoppel, strictly speaking, applies only to matters of record, so that the court in its opinion was using the word estoppel either in a sense of equitable estoppel or quasi estoppel, and in this argument we will not spend too much time in distinguishing between the application of estoppel, equitable estoppel or quasi estoppel. Although the latter term is probably more accurate in view of the acts considered by the court of appeals in support of its contention that petitioner is not entitled to recover.

The most important matter under consideration in this case is one of law. The district court first held that receipt of partial payments by petitioner from the corporation on the indebtedness of the partnership to petitioner shows an acquiescence and amounted to estoppel. We contend that making said payments did not show acquiescence and did not amount to an estoppel.

The agreement between the partnership and the corporation whereby the latter acquired the assets of the former and assumed and agreed to pay the debts and obligations of the partnership, which included, of course, the obligation due to petitioner and the other eighteen creditors, similarly situated, was an offer in novation, and that the law applicable on whether or not a novation was established by the corporation making the two subsequent partial payments on the indebtedness of the partnership to petitioner. That question is definitely settled by the decisions of the Supreme Court of the State of Illinois.

In *Walker* v. *Wood*, 170 Ill., 463, a partnership known as James H. Walker and Co., owed to appellee Wood and others $1,739.98 for goods purchased. The partners of the partnership organized a corporation under the name of J. H. Walker Co., and the corporation acquired the assets of the partnership and assumed the liabilities of the partnership. Subsequently the appellee received from the corporation a payment of $500.00, which it applied on the debt of the partnership, which the corporation had assumed and agreed to pay. Later the corporation became insolvent and a receiver was appointed for it, before whom appellee proved his claim alleging the indebtedness of the firm, and that the corporation had assumed and agreed to pay the same. Thereafter appellee brought a suit against the members of the firm. Dividends in the sum of $892.79 were paid on said claim by the receiver of the corporation. The partners filed a plea alleging that the corporation had assumed and agreed to pay appellee, the amount of their claim, and that appellees had accepted the said promise of the corporation, and thereby released the members of the original firm from all liability. The case was tried before the court without a jury and a finding and judgment was rendered against the partners of the partnership for the unpaid balance claimed due to appellee. The ap-

pellate court affirmed the judgment of the trial court, and granted its certificate of importance by virtue of which appellant, the partnership brought the cause to the Supreme Court of Illinois. The Supreme Court of Illinois in disposing of the question at page 467 said:

> "We regard the modification as correct. The assumption of outstanding liabilities by the corporation was a matter of agreement between it and the defendants, which could not affect the rights of the plaintiffs unless they assented to it in some way which amounted to an agreement to accept the corporation as alone liable for the indebtedness. It is essential to a novation that all the parties to the contract for which the new one is substituted consent to it. (16 Am. & Eng. Ency. of Law, 867; *Hayward* v. *Burke,* 151 Ill. 121.) The assent or agreement may be either express or implied, but neither knowledge of the arrangement between the corporation and the firm, nor the partial payment of the debt, nor a demand for the payment, like the filing of the claim against the corporation, nor all combined. necessarily establishes such assent or agreement as a legal conclusion. (16 Am. & Eng. Ency. of Law, 904; *Rayburn* v. *Day,* 27 Ill. 46; *Goodenow* v. *Jones,* 75 id. 48; *Hayward* v. *Burke, supra.*)"

The *Walker* case, *supra,* was proved and followed by the Supreme Court of Illinois in the comparatively recent case of *Burnett* v. *West Madison State Bank,* 375 Ill. 402. In that case the plaintiff appellant was a depositor in the West Madison State Bank in Chicago, Illinois, and when it was in failing circumstances it was consolidated with the Garfield State Bank also a state banking institution located in the City of Chicago, and doing business in the State of Illinois. At the time of said consolidation, the Garfield State Bank assumed and agreed to pay all the debts and obligations of the West Madison State Bank. Later the Garfield State Bank was closed by the auditor

of public accounts of said state on June 11, 1931, without having paid all the indebtedness of the West Madison State Bank. A receiver was appointed for the Garfield State Bank and the liquidation of its assets was started. During the liquidation proceedings, payments were made by the receiver of the Garfield State Bank on the amount due by the West Madison State Bank to appellant, who was its depositor. Appellant thereafter filed a complaint in the Circuit Court of Cook County against the West Madison State Bank to enforce the superadded liability of the stockholders fixed by the statutes of the State of Illinois. The said suit was prosecuted as a representative action for the benefit of all of the creditors of the West Madison State Bank. The first question raised as a defense to the suit brought by the said depositor against the West Madison State Bank was that the Statute of Limitations had run before the suit was filed. The trial court sustained the Statute of Limitations as a defense to the suit and appellant in this case thereafter removed the case to the Supreme Court of Illinois. The Supreme Court of Illinois in its decision in that case first held that the Statute of Limitations had not run and then disposed of the second issue in the case which was very much like the questions here under consideration. At pages 409 and 410 of the opinion in that case, the court said:

> "The second ground assigned by the appellee for dismissal of the suit is based on two propositions only slightly variant. The primary conception of appellee's contention under this point is that when the West Madison State Bank was consolidated with the Garfield State Bank the liabilities of the former bank were assumed by the latter and that, by operation of law, such consolidation extinguished any further liability of the West Madison State Bank or its stockholders to the creditors of the bank. The appellee further says that, after the consideration, the creditors of the West Madison State Bank looked to the consoli-

dated bank for payment of their claims and their conduct in accepting dividends on their deposits from the receiver appointed to liquidate the Garfield State Bank, and the delay in waiting nearly eight years before asserting their claims against the stockholders of the West Madison State Bank, did, as a matter of law, work a novation and constituted the Garfield State Bank and its stockholders appellant's debtors, and that the West Madison State Bank and its stockholders were thereby discharged from further liability.

To constitute novation by substitution of debtors, it is essential the creditor shall have consented to the substitution of a new debt and debtor and shall have agreed to release his original debtor and to accept in his stead the new party. (*Commercial Nat. Bank* v. *Kirkwood,* 172 Ill. 563; *Kiefer* v. *Reis,* 331 id. 38; *Hayward* v. *Burke,* 151 id. 121.) Assent of the creditor to the novation may be implied from facts and circumstances attending the transaction or from the subsequent conduct of the creditor (*Walker* v. *Wood,* 170 Ill. 463; *Hayward* v. *Burke, supra;*) but no facts are alleged in this complaint from which a novation can be implied. The mere consolidation of the banks, and the continuance of appellant's deposit with the new bank together with his acceptance of dividends in the liquidation proceedings and the delay in pressing his claim against the stockholders of the old bank, do not constitute a novation as a matter of law. (*Walker* v. *Wood, supra; Hayward* v. *Burke, supra.*) Novation is never presumed. It is an affirmative defense and must be proved by clear and competent legal evidence." See *Northwestern Mutual Life Ins. Co.* v. *Eddleman,* 247 Ky. 116, 56 S. W. (2d) 561, 87 A. L. R. 276.

The *Walker* case, and the *Burnett* case, and the other cases cited and relied on in those cases definitely establish the law of the State of Illinois on the question of novation and have definitely decided that when one receives part payment on his debt made by another who has assumed and agreed to pay the debts of the original debtor, and when

said payments are received with knowledge of the fact that the new debtor has assumed the obligations of the old debtor, that this does not effect or accomplish a novation so far as the creditor is concerned, and thereby release the old debtor from its obligation. Under such circumstances the creditor may not only receive payment but enforce payment from either or both of its debtors. If such be the law, then accepting part payment from either could certainly not work an estoppel, and the court of appeals, in this case has, therefore, disregarded the well settled law of the State of Illinois on the subject by applying the doctrine of estoppel as a defense to petitioner's claim for reclamation.

The decisions of the Supreme Court of Illinois, as announced in *Walker* v. *Wood* and *Burnett* v. *West Madison State Bank, supra,* and the decisions in the other cases in the State of Illinois, therein cited, establish the rule that where the partnership transferred its assets to the corporation, and the corporation, in consideration therefor, assumed and agreed to pay the debts and obligations of the partnership, constituted an offer in novation to all of the creditors of the partnership, of which petitioner in this case was one. Said cases have further settled the law in Illinois, that merely accepting payment from the corporation on a part of its debt, even when petitioner knew of all the facts surrounding the sale and assumption of such indebtedness, does not release the original obligor from the payment of its debts. If accepting payment with such knowledge did not under the settled law of Illinois release either the partnership from the payment of the obligations of the partnership to petitioner, then the application of the doctrine of estoppel as a defense to this suit was erroneous.

The instant case is even a stronger case than either the *Walker* case, *supra,* or the *Burnett* case, *supra,* or any of the cases therein cited, laying down the rule, because Mr.

Fisher, the president of petitioner bank, testified that he had always retained the two promissory notes JJ2, $17,900.00 and JJ3 for $14,000.00, totaling $31,900.00 and relied upon as the basis for petitioner's claim for reclamation (R. 86). He further testified that he had at all times refused to surrender them to anyone because they were signed by the partnership and by Gill and Owen, individually, and that he did not want to surrender the obligations of the partnership and thereby release said sureties from the payment of the same (R. 83). In the instant case, however, petitioner has disproved all intentions of releasing the partnership from the payments of its obligation, and Mr. Fisher's testimony on said question is not disputed. It is held in the case of *Burnett* v. *West Madison State Bank, supra,* that "In the absence of clear proof of novation the fact of consolidation (including the assumption of the indebtedness) would make the Garfield State Bank an additional debtor and by accepting part payment from the additional promissor, the claim would not be relinquished against the former bank, the liability of its stockholders thereby discharged." In that case it was further held, that a claim of novation is an affirmative defense and must be proved by clear and competent legal evidence. The burden was, therefore, upon the corporation in this case to prove that the acts relied upon constituted a release of the obligations of the partnership to petitioner. As above stated, the court has held that mere knowledge of the surrounding acts does not constitute proof of such release.

The court of appeals erred in not following the well settled law of the State of Illinois on this question. The court of appeals on the contrary, first, followed the decision of the district court on the question of the application of estoppel as a defense to this suit, which cited no authority whatever in support of its decision. Second, the court

of appeals erred in relying on a general rule or headnote found in 15 A. L. R. 2nd 937, which said annotation cited no decisions of the Supreme Court of the State of Illinois, and only based its assumption of what the law on the decisions of the courts of foreign states, and two decisions of the appellate court of which state, which is an inferior court. Some of the decisions of other states and the appellate court of this state held, however, under the particular facts that estoppel might be applied, while in others it was denied, but regardless of this fact the decision of the lower court, and the law stated in said headnote, both of which were contrary to the well established rule of Illinois, should not have been followed.

The court of appeals should have followed the rules well settled by the decisions of the Supreme Court of Illinois, as required by the rule announced in *Erie R. Co.* v. *Tompkins,* 304 U. S. 64, 83 L. Ed. 1188, and since followed by many decisions by said court, holding that the court of appeals must apply the rule of law announced by the decisions of the highest court of the state to be the law governing all transactions, rather than consider the decisions of cases of other states for the purpose of determining for itself what the law is or should be. The failure or refusal of the court of appeals in this case to comply with the rules of the decisions in said *Erie R. Co.* v. *Tompkins* and other cases since decided, is, therefore grounds for the granting of this Writ of Certiorari to review the decision of the court of appeals under Rule 38 (5-b), which among other things provides: "that where a court of appeals has decided an important question of local law in a way probably in conflict with applicable local decisions or has so far sanctioned such a departure by a lower court as to call for an exercise of this court's power of supervision."

B. The Corporation Had Knowledge of the Fact that It Had Assumed and Agreed to Pay the Debts of the Partnership. In Making Payments on Its Agreement and the Acceptance of Such Payments by the Petitioner Did Not Mislead It in the Least. Unless It Was Misled in Some Manner With Reference to the Facts, Neither Estoppel, Equitable Estoppel, Nor Quasi Estoppel Are Available to It as a Defense.

The estoppel relied upon by the Court of Appeals as a defense to petitioner's suit is not an estoppel at all. The estoppel relied upon should evidently have been designated either as an equitable estoppel or a quasi estoppel, but neither equitable estoppel nor quasi estoppel constitute a defense to petitioner's right to recover under it, petition for reclamation, 19 Am. Jur. 692, Section 65 "Estoppel"; See also *Grand Trunk, Etc.*, v. *Nelson* 116 Fed. 2nd 22, opinion by Judge Kerner, concurred in by Judges Evans and Major of the United States Court of Appeals for the Seventh Circuit, in which certiorari was denied by this Court, 232 U. S. 761, 89 L. Ed. 609. If we treat the acceptance of payments as being quasi estoppel then the same rule applies against its application here because estoppel is only a defense when the party claiming the estoppel is without knowledge or means of the knowledge on which he bases his claim of estoppel. 31 C. J. S. 349 estoppel Section 109 (b).

Under these rules the corporation could not plead estoppel as a defense to the suit filed for reclamation because the corporation was charged with full knowledge of all the terms and conditions of the contract which it assumed and agreed to pay and therefore, knew when it was making these payments it was doing what it had agreed to do. It had equally as much knowledge as petitioner did concerning the facts.

C. Petitioner Was Not Estopped Even By the Application of Quasi Estoppel From Receiving Said Payments On Its Debt, Because the Doctrine of Estoppel Never Applies When One Is Only Receiving That Which He Is Legally Entitled to Receive in All Events.

The corporation for good and valuable consideration has assumed and agreed to pay the debts and obligations of the partnership, including the sum of $34,500 due to petitioner. The corporation in making said payments totaling $2,600 on the indebtedness of the partnership to petitioner was complying with its agreement, and in making said payments, the corporation was only receiving and accepting what it was legally entitled to receive in any event, and receipt of said payments under such circumstances does not constitute estoppel. 19 Am. Jur. 692, Section 65, under the subject of "Estoppel"; see also *Grand Trunk, etc.* v. *Nelson,* 116 Fed. 2d 22, opinion by Judge Kerner, concurred in by Judges Evans and Major of the United States Court of Appeals for the Seventh Circuit, in which certiorari was denied by this Court, 232 U. S. 761, 89 L. Ed. 609. The same rule applies whether the estoppel relied upon was technical estoppel, equitable estoppel, or quasi estoppel. 31 C. J. S. 350 Estoppel Sec. 109 (b).

Under the rule of law above stated, accepting payments, under such circumstances and when it was only obtaining that to which it was legally entitled to receive in all events, the defense of estoppel, equitable estoppel and quasi estoppel were not defenses and certiorari should be granted.

Conclusion.

It is, therefore, respectfully submitted that this case is one calling for the exercise by this Court of its supervisory powers by granting a Writ of Certiorari, and thereafter reviewing and reversing said decision.

Dated this 23rd day of September, A. D. 1953.

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APPENDIX.

The Opinion of the United States Court of Appeals for the Seventh Circuit rendered May 20, 1953, In the Matter of the Gill-Owen Company, Bankrupt; The Hillsboro National Bank, Appellant v. *J. Paul Buscher, Trustee, Appellee, is as follows:*

"Before DUFFY, FINNEGAN and LINDLEY, *Circuit Judges.*

FINNEGAN, *Circuit Judge.* On June 14, 1950, the Hillsboro National Bank filed its petition for reclamation in the bankruptcy proceedings of The Gill-Owen Company, voluntary bankrupt. Eighteen other persons, firms and corporations likewise filed reclamation petitions in the same matter, some on the same day, June 14, 1950, and others shortly before or after that date.

In the various petitions, the petitioners alleged that they were creditors of a co-partnership doing business as Litchfield Precision Products, the partners being one David E. Owen and one E. A. Gill. The petitioners sought to reclaim all of the stock of merchandise, or merchandise and fixtures or other goods and chattels which they alleged had been sold by Litchfield Precision Products to The Gill-Owen Company, a corporation, on August 13, 1948, otherwise than in the ordinary course of trade. Lists of the goods and chattels sought to be reclaimed were attached to the petitions. The petitions charged that the property sold to the corporate bankrupt on August 31, 1948, embraced substantially all of the assets of the partnership, Litchfield Precision Products. The petition further alleged that the various petitioners, creditors of the partnership had not been given written notice of the sale as required by the Bulk

Sales Act of the State of Illinois (Smith-Hurd Ill. Ann. Stat., Ch. 121½, sec. 78, *et seq.*) and that as a consequence said sale of August 31, 1948, was void as against petitioners, and that the assets then sold belonged to the petitioners.

In its brief in this Court, appellant states that by agreement of all the parties, the outcome of all other reclamation petitions, except that of D. E. Owen, would abide by the result and decision arrived at on the petition of the Hillsboro National Bank. We therefore limit our consideration to that petition, the answer of the Trustee in Bankruptcy thereto, and the facts disclosed on the hearing thereof.

In answer to appellant's petition the Trustee in Bankruptcy, after a general denial of the allegations in the petition, alleged that the sale and transfer of the goods and chattels from Litchfield Precision Products to the corporate bankrupt, on August 31, 1948, was not such a transfer as required compliance with the Bulk Sales Act of Illinois. The answer further claimed that if said Bulk Sales Act were held to apply to said sale, the petitioner-appellant had waived its rights to complain of said sale because: (1) appellant has been guilty of laches; (2) it affirmed said sale by accepting the terms thereof which provided that The Gill-Owen Company assumed and agreed to pay all the debts of Litchfield Precision Products, and that petitioner with full knowledge of the facts has accepted payment from the corporate bankrupt on the indebtedness of said partnership and has thereby ratified and confirmed the sale of August 31, 1948, and (3) that under the facts and circumstances the appellant is estopped from recovering the goods and chattels transferred and that appellant has filed its claim against the corporate bankrupt, participated in the selection of a trustee and has made frequent appearances in the bankruptcy proceeding.

The matter was first heard by the Referee in Bankruptcy who found in favor of the petitioners in reclamation and ordered that the proceeds of the sale (in bankruptcy) of the goods and chattels transferred on August 31, 1948, amounting to $20,546.33, less costs of administration, should be distributed to the petitioners in reclamation in due course of administration. The Trustee in Bankruptcy petitioned for a review of the referee's order and prayed that the entire record be certified to the District Court.

After consideration of the record and of the briefs and arguments submitted by the parties involved, the District Judge held that the reclamation petitioners were not entitled to the proceeds of the sale of the goods and chattels transferred, but should be treated as general creditors of The Gill-Owen Company. An order to that effect was entered by the District Judge on July 30, 1952. Motions for a new trial and for reconsideration were entered and denied on August 28, 1952. This appeal followed.

A brief statement of the facts disclosed by the record, which are practically undisputed, will aid in the consideration and appraisal of the contentions presented by the appellant and by the appellee.

Early in 1941, David E. Owen, with his wife and one E. A. Gill, formed a partnership, calling it Litchfield Precision Products. In the partnership Owen owned a 40% interest, his wife a 20% interest and Gill a 40% interest. Owen later acquired the interest of his wife. The partnership acquired precision machinery and obtained contracts for war purposes.

In September of 1945, Gill and Owen, along with other small stockholders, incorporated The Gill-Owen Company. This company was organized as a sales agency for the Litchfield Precision Products. On August 31, 1948, the Litchfield Precision Products, the partnership, sold to Gill-

Owen Company, the bankrupt herein, 95% of its assets. This was done in order to reduce the office force and overhead expense, and as a part of said transaction Gill-Owen Company assumed and agreed to pay all partnership indebtedness.

Gill and Owen were advised that since they were partners and owned all the interest in the partnership and substantially all the stock in the corporation, and since they expected to pay all the obligations of both, there was no need for them to comply with the Bulk Sales Act in selling and transferring the assets of the partnership to the corporation. Therefore neither the partnership nor the corporation gave any notice to the creditors of the Litchfield Precision Products, the partnership, of the intended sale. No attempt was made by either to comply with the provisions or requirements of the Bulk Sales Law of the State of Illinois.

The record does however show positively that the Hillsboro National Bank did, at or about the time of the transaction, have actual knowledge of the transfer of the goods and chattels involved by the partnership to the corporate bankrupt. The partners advised and consulted with the president of the bank. Both the partnership Litchfield Precision Products and The Gill-Owen Company, Incorporated, maintained checking accounts with the bank. As a matter of fact the record discloses that after the transfer of the partnership assets to the corporation, payroll checks were issued on Litchfield Precision Products check forms and were honored and paid by the bank with funds furnished by The Gill-Owen Company for a payroll account. It was claimed that this was done because the Litchfield partnership had a large number of such forms, which had been printed on the firm's order, still on hand and it would have been wasteful not to use them. This practice continued until 1949.

Moreover, it appears that the bank was acquainted with every detail regarding the financial standing of the copartnership and of The Gill-Owen Company. The president of the bank visited the plant of the company saw and examined the machinery. He inquired and was told the names of the attorneys who were handling the transfer. The bank also transferred the account of Litchfield Precision Products to The Gill-Owen Company.

At the time of the hearing the bank had in its possession and produced two notes signed by the Litchfield Precision Products and the co-partners. One for $14,000 was dated March 27, 1949, and the second for $17,900 was dated June 24, 1949. There were renewal notes evidencing the indebtedness of the partnership to the bank on August 31, 1948.

The bank likewise produced at the hearing two notes of The Gill-Owen Company, one for $14,000 dated August 27, 1949, and the other for $17,900 dated August 24, 1949. The president of the bank testified that these latter notes were never used, never went into the bank. They were taken because Gill-Owen was to obtain new capital but failed. They never paid interest on these notes.

Finally the bank took a note for $16,900, dated November 17, 1949, signed by The Gill-Owen Company and secured by a chattel mortgage and also a note of the company for $30,000 dated November 26, 1949, and secured by a real estate mortgage which is stated to be unrecorded.

The record further discloses that the bank was paid $2600 by The Gill-Owen Company on the partnership indebtedness of August 31, 1948. It likewise appears that The Gill-Owen Company in discharge of its promise to assume the partnership debts had paid to creditors, other than the bank, sums aggregating from $12,000 to $14,000.

The appellant claims that the transfer to the corporate

bankrupt by the partnership was void under the Illinois Bulk Sales Act, and that the order appealed from should be reversed and the order of the referee should be reinstated.

Appellee contends that the Illinois Bulk Sales Act was not applicable to the transaction of August 31, 1948. It then urges that even if said act is applicable, the petitioner, under the facts and circumstances shown by this record, is estopped to avoid such transaction and has lost by waiver any right to upset it.

In stating the reasons which impelled him to conclude that the petitioners in reclamation were not entitled to the proceeds of the sale of the goods and chattels transferred by a partnership to The Gill-Owen Company, but that they should be treated as general creditors of the corporate bankrupt, the trial court said:

> "Under such circumstances I think it extremely doubtful whether the Bulk Sales Act applies; but I shall not labor that question as I am fully convinced that the bank, having acquiesced in the sale and received the benefits therefrom, is not now in a position to prevail in their reclamation petition. The bank accepted the benefits of the transfer knowing all the facts, and later when bankruptcy intervened, filed their claim against the corporation as a general creditor. Now at a later date they are seeking to the exclusion of general creditors to impress a lien on the property transferred to the corporation by the co-partnership on the theory of non-compliance with the Bulk Sales Act. The bank evidenced satisfaction with the transfer although they received no written notice as provided by the Act, cooperated with the transferrer and the transferee in an effort to liquidate their claim and did in fact partially liquidate the same with money which the corporation received and paid them as a direct result of the operations under the transfer. The bank accepted the benefits of the transfer as long as benefits were forthcoming, but now that benefits have ceased and bank-

> ruptcy intervened they are asserting that the transfer was at all times void. To permit them to thus gain what advantages could be had by reason of the transfer and then later assert a claim to the property thus transferred because of a failure to give notice under the Bulk Sales Act would permit the Bulk Sales Act to become an instrument of fraud rather than one of protection of creditors. The reclamation petitioner does not come into this, a court of equity, with clean hands."

We agree with the conclusions reached by the trial court and believe it is supported by overwhelming competent authority.

15 A. L. R. (2d) on page 937 contains an annotation entitled: "Waiver, Estoppel, Acquiescence or Laches of creditor with respect to attack on sale under Bulk Sales Act." On page 939 of said annotation, it is said:

> "It appears to be well settled that creditors may waive the right to the benefit of the Bulk Sales Statutes, or estop themselves to claim that the sale was invalid because the requirements of the Bulk Sales Statute were not fully complied with."

The editors cite decisions from courts of review in sixteen of the States and from the Dominion of Canada in support of this proposition. Tow of the cases cited are from the Appellate Court of Illinois: *Jeffrey Hotel Corp.* v. *Chicopulos,* 262 Ill. App. 537, and *Marshall Co.* v. *Leon,* 267 Ill. App. 242.

In the *Jeffrey Hotel* case, which was decided in 1931, it developed that a garnishee had purchased hotel furniture in violation of the Bulk Sales Act of Illinois. The evidence disclosed that the plaintiff, who was the holder of a chattel mortgage upon the furniture sold, had agreed to a general compromise of the seller's obligations. The court held that the plaintiff was estopped from claiming a violation of the Bulk Sales Act by the garnishee.

In *Marshall Co.* v. *Leon*, which was decided in 1932, it held that a creditor who affirmatively consents to the sale by his debtor of a stock of merchandise, is not entitled to claim that the sale was fraudulent and void because there was a failure to give notice as required by the Bulk Sales Act of Illinois. This case was cited with approval in *Brady* v. *Marshall*, 302 Ill. App. page 151, which was decided in 1939. In the *Marshall* case the Appellate Court reversed a judgment for a creditor because of the exclusion of evidence. It said on page 158:

> "* * * In the absence of this evidence we will not pass on the question of whether it was sufficient to create an estoppel, although it would seem on principle plaintiff would be estopped to complain that notice was not given under the Bulk Sales Act, if he in fact participated in and took the benefits of a transaction with full knowledge that such notice was not given."

The order and judgment of the District Court is affirmed.

Section 1 of the Bulk Sales Act of the State of Illinois, being paragraph 78, Chapter 121½ of Illinois Revied Statutes, 1947, Bar Association Edition, and also found in Smith-Hurd Annotated Illinois Statutes, in the same section, paragraph and chapter, is as follows:

The sale, transfer, or assignment in bulk of the major part or the whole of a stock of merchandise, or merchandise and fixtures or other goods and chattels of the vendor's business, otherwise than in the ordinary course of trade and in the regular and usual prosecution of the vendor's business is fraudulent and void as against the creditors of the vendor, unless the vendee shall, in good faith, at least ten (10) days before the consummation of the sale, transfer or assignment demand and receive from the vendor a written statement under oath of the vendor or a

duly authorized agent of the vendor having knowledge of the facts, containing full, accurate and complete list of the creditors of the vendor, their addresses and amounts owing to each as near as may be ascertained, and if there be no creditors a written statement under oath to that effect; and unless the said vendee shall at least ten days before taking possession of said goods and chattels and at least five days before the payment or delivery of the purchase price, or consideration or any evidence of indebtedness therefor, in good faith, deliver or cause to be delivered or send or cause to be sent personally or by registered letter properly stamped, directed and addressed, a notice in writing to each of the creditors of the vendor named in the said statement or of whom the said vendee shall have knowledge, of the proposed purchase by him of the said goods and chattels and of the price, terms and conditions of such sale; Provided, however, that it shall be lawful for the vendee to pay to the vendor so much of the purchase price as shall be in excess of the total amount of the indebtedness of the vendor, before the expiration of the ten days hereinbefore referred to.

Section 3 of the Bulk Sales Act of the State of Illinois, being paragraph 80, Chapter 121½ of Illinois Revised Statutes, 1947, Bar Association Edition, and also found in Smith-Hurd Annotated Statutes, in the same section paragraph and chapter, is as follows:

Vendors and Vendees under this act shall include corporations, associations, co-partnerships and individuals, who shall be party to any sale, transfer or assignment, of goods and chattels in bulk. But nothing contained in this act shall apply to sales by executors, administrators, receivers, trustees in bankruptcy or by any public officer under judicial process nor to sales of exempt property or any sale or transfer made in the ordinary course of trade

and in the regular and usual prosecution of the vendor's business nor to sales made in good faith at public auction, where notice of such sale is given in a newspaper of general circulation within the county where such sale is made, at least ten days before such sale or by posting of notices in at least five public places at least ten days before said sale.

Section 4 of the Bulk Sales Act of the State of Illinois, being paragraph 80a, Chapter 121½ of Illinois Revised Statutes, 1947, Bar Association Edition, and also found in Smith-Hurd Annotated Statutes, in the same paragraph and chapter, is as follows:

Any creditor or creditors of the vendor of any stock of merchandise, merchandise and fixtures, or other goods and chattels of the vendor's business made in violation of the provisions of this act, may pursue his remedy either at law or in equity, against either the vendor or vendors, the purchaser or purchasers, jointly or severally, or against the whole or any part of such stock of merchandise, merchandise and fixtures, or other goods and chattels, by a suit either at law or in equity, without having reduced his claim to judgment; and the court in which said suit is pending shall have jurisdiction to adjust the rights and equities of all parties having an interest in the property in such proceedings.

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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1953.

No. 365

IN MATTER OF THE GILL-OWEN COMPANY,
BANKRUPT.

THE HILLSBORO NATIONAL BANK,
Petitioner,

vs.

J. PAUL BUSCHER, TRUSTEE IN BANKRUPTCY OF THE ESTATE OF THE GILL-OWEN CO., A BANKRUPT,
Respondent.

ANSWER OF RESPONDENT, J. PAUL BUSCHER, TRUSTEE IN BANKRUPTCY OF THE ESTATE OF THE GILL-OWEN CO., A BANKRUPT, TO THE PETITION OF THE HILLSBORO NATIONAL BANK FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT AND BRIEF AND ARGUMENT IN SUPPORT OF THE ANSWER.

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THE GUNTHORP-WARREN PRINTING COMPANY, CHICAGO

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STATEMENT.

The statement of the facts and chronological history of the proceedings in the brief and argument for petitioner are substantially correct so far as stated, but are insufficient to present all the issues involved. I, therefore, desire to add to the same some of the other pleadings and facts

shown in the record not referred to by petitioner in its brief and argument.

It is nowhere stated in the brief and argument of petitioner that the answer filed by defendant (R. 11) denied that the sale and transfer of the personal property of Litchfield Precision Products (the partnership) to The Gill-Owen Company, the present bankrupt, was such a transaction as required a compliance with the Illinois Bulk Sales Law. This was an issue before the Referee and in the District Court and United States Court of Appeals. Evidence was heard on the question before the Referee and briefs filed there and in the District Court and United States Court of Appeals and I desire to present that question in opposing the granting of the petition for writ of certiorari in this case. The evidence as to the transfer or reorganization will be found in the testimony of Edmund A. Gill, a partner in the Litchfield Precision Products (R. 96-97-98, 102, 103-105, 108-110), also of Mr. Fisher, president of the petitioner bank (R. 64, 67-70-73), Juanita Goff (R. 51-53-57) and David E. Owen (R. 22, 25-26-27, 28, 36-37). I rely on this evidence to sustain my contention that the transfer from the partnership to the same persons owning the corporation, The Gill-Owen Company, did not require compliance with the Illinois Bulk Sales Law and did not require written notice of the transfer. Having had full knowledge of the transaction and having actively participated in perfecting the change-over to The Gill-Owen Company, much to the petitioner bank's advantage, no notice was required.

The statement of petitioner omits the fact that Mr. Fisher, the president of the bank, had knowledge of the transfer of the personal property from the partnership to the corporation before, at the time, and immediately after the transfer was made on August 31, 1948.

I dislike to lengthen this answer by quoting from the

record. In view, however, of the fact that no reference is made to the same in petitioner's statement and its knowledge of the same is minimized in the argument, I refer briefly to the testimony of Mr. Fisher, the president of the bank (R. 70-72), in which he testified that Mr. Gill (one of the partners and one of the owners of the corporation) talked to him about the transfer. Fisher said it was a day or two afterwards of August 31, the day of the actual transfer. Mr. Fisher himself testified (R. 67) concerning the transfer that "They told me that they were going to and I asked them about it at the time, and I asked them who was representing them and they said their attorneys were making the transfer;" and to the specific question, "You knew it, didn't you?" answered "Yes, sir."

Mr. Edmund A. Gill (R. 99) testified that before the merging of the two companies he talked with Mr. Fisher at the bank, telling him of their plan for the Litchfield Precision Products to sell to The Gill-Owen Company and thereby cut down its expenses, and for other reasons noted, and that he had discussed the proposed transfer with Mr. Fisher on several occasions, both he and Mr. Owen talking with him.

Mr. Owen testified (R. 34) that he informed The Hillsboro National Bank of the transaction "within two or three days after September 1."

Mr. Gill (R. 110) further stated, referring to a conversation with Mr. Fisher, that "We discussed it (the transfer) in person—the advisability of what to do in absorbing the Litchfield Precision Products into Gill-Owen."

Juanita Goff, a bookkeeper of the partnership and of the corporation, testified (R. 50) that after August 31, 1948 the payroll continued under the name of the partnership until new checks were acquired and was paid by the petitioner bank upon checks issued by the partnership

subsequent to that day when a combined account was opened by the partnership and the corporation (R. 51) and checks were issued in the name of the partnership against the Gill-Owen account up to August, 1949 (R. 52).

I further call attention to the statement of Mr. Fisher (R. 82) that on August 31, 1948, the date of the transfer from the partnership to the corporation, two of the notes upon which this claim is partially based, in the sum of $31,900.00 were executed by Litchfield Precision Products and The Gill-Owen Company and delivered to him at the bank and that he had at the time of giving his testimony the same two notes and that they represented the amount due to the bank at the time the assets were transferred to The Gill-Owen Company on August 31, 1948, and that he, representing the bank (R. 83), yet has the same notes; that they were given for the purpose of renewal.

Further (R. 84), he was thereafter told that from $25,000.00 to $35,000.00 additional money was to be put into the business and that he, Fisher, consulted with Mr. White, a lawyer and director of the bank, concerning the taking of a chattel mortgage to further secure the indebtedness and that an overdraft of $8,920.73 (R. 85) existed and was to run along until the new capital was put in and that on August 23, 1949 $9,500.00 was deposited, which cleared this overdraft and left some remaining. This was all after he, Fisher, as president of the bank, had full knowledge of the transfer of the personal property and that the two notes are the only evidence on the claim which the bank is presenting and form the basis of a large part of the reclamation claim (R. 86).

Fisher further testified (R. 89) that interest was paid by The Gill-Owen Company on the notes, the amount not being specified; that the partnership name was not on the notes but they were all signed by The Gill-Owen Company after the transfer.

Mr. Fisher further testified (R. 90) that Mr. Gill or Mr. Owen told him soon after the "transfer, sale or absorption" of the partnership by The Gill-Owen Company that the corporation had assumed and agreed to pay all of the Litchfield Precision Products claims; that the bank took a note on November 17, 1949 for $16,900.00 secured by a chattel mortgage and three notes for $15,000.00, $14,000.00 and $17,900.00 signed by The Gill-Owen Company and that the bank filed the $30,000.00 real estate mortgage note (R. 94).

Fisher further testified (R. 76) that under date of September 15, 1949 a deposit was made in the bank for $8,191.20 by The Gill-Owen Company. This, with the $2,600.00 referred to in petitioner's statement and the other payments shown in the record, brings the amount received by The Hillsboro National Bank, petitioner, from The Gill-Owen Company, the corporation, after the transfer of the personal assets and before it filed its reclamation claim to the sum of $20,291.20 instead of the $2,600.00 referred to by Attorneys for petitioner in their statement. In addition to the amount that was received by The Hillsboro National Bank, the petitioner, there was also received from The Gill-Owen Company after the transfer and before bankruptcy by the other seventeen reclamation claimants the sum of $11,622.08 (R. 117). The total amount received by all reclamation claimants from the respondent bankrupt estate, instead of being $2,600.00, as stated by attorneys for the petitioner, is the sum of a little more than $31,900.00, omitting considerable interest, the amount not being specified which was received, after full knowledge that the transfer of the personal property from the partnership was made to the corporation.

REASONS WHY THE WRIT OF CERTIORARI SHOULD NOT BE GRANTED.

(a) No federal question is involved and there is no decision of a state court contrary and not in accord with the decisions of this court.

(b) The decision in this case is not in conflict with the decision of another United States Court of appeals on the same matter.

(c) The decision is not in conflict with any local law or applicable local decisions.

(d) There is no important question of federal law which has not been decided that should be settled by this court.

(e) The decision is not in conflict with applicable decisions of this court.

(f) The decision has not departed from the accepted and usual course of judicial proceedings, or so far sanctioned such a departure by a lower court as to call for an exercise of this court's power of supervision.

CONTESTED ISSUES.

There are really only two contested material issues in this case.

1. Was the sale or transfer of the partnership property of Litchfield Precision Products fraudulent and void as to petitioner because of the failure to comply with the provisions of the Illinois Bulk Sales Law and for that reason is petitioner entitled to a prior or preferred claim on the personal property under its reclamation claim?

2. If the transfer was void for failure to comply with the provisions of the Illinois Bulk Sales Law, then has the petitioner lost its claim to a prior or preferred claim or lien on the personal property by reason of waiver, laches or delay, ratification or estoppel or by accepting payments on its indebtedness or by participating in the bankruptcy proceedings as alleged in the answer of respondent?

BRIEF.

1. The sale or transfer of the personal property of Litchfield Precision Products, the partnership, to The Gill-Owen Company, the bankrupt corporation, in the manner shown by the evidence was such that it was not necessary to comply with the Illinois Bulk Sales Law by giving written notice thereof to the petitioner, The Hillsboro National Bank.

McLean v. *Miller Robinson Co.*, 55 F. 2d 232.
Thorpe v. *Pennock Mercantile Co.*, 99 Minn. 22.
Also reported in American and English Annotated Cases Vol. 9, page 229.
Maskell v. *Spokane*, 100 Wash. 16.
Also reported in L. R. A. 1918C, page 929.
24 American Jurisprudence, Sec. 240, page 352.
24 American Jurisprudence, Sec. 255, pages 360-361.

2. The petitioner having had actual knowledge of the transfer or sale of the personal property of Litchfield Precision Products and having participated in making the sale and having received benefits and payments thereunder is estopped to now claim a prior and preferred lien on the same and is barred by ratification, waiver and laches from sharing in the proceeds only as a general creditor.

C. & E. Marshall Co. v. *Leon*, 267 Ill. App. 242.
Jeffry Hotel Corp. v. *Chicopulos*, 262 Ill. App. 537.
Aaron v. *Dausch*, 313 Ill. App. 254.
Brady v. *Marshall*, 302 Ill. App. 151.
Milwaukee Commercial Bank v. *Bennett*, 249 Ill. App. 456.
Gilbert Collier on Bankruptcy, 2d., page 1220.

Bouvier's Law Dictionary, 12 Ed., Vol. 1, page 541.

3. The Bulk Sales Law was adopted for the protection of all creditors of the seller. A statutory provision (Bulk Sales Law) that, in the absence of compliance therewith, a sale in bulk shall be "void" as against creditors of the seller, means that the sale shall be voidable.

15 A. L. R. (2) 925.

4. The rules of law as to a novation are not applicable and are not an issue in this case in this court.

39 American Jurisprudence, Sec. 2, page 255.

39 American Jurisprudence, Sec. 19, page 264.

ARGUMENT.

I.

The Sale and Transfer of the Personal Property of Litchfield Precision Products to The Gill-Owen Company, a Corporation, the Bankrupt, Was Not Such a Transaction as Required Compliance With the Illinois Bulk Sales Law.

It is not practicable for the respondent to discuss the points at issue in the order they appear in the brief for petitioner. That is because counsel for petitioner have not discussed the question raised by the Trustee's answer to the reclamation claim of the petitioner filed in the office of the Referee in Bankruptcy on June 22, 1950. I consider this issue material and vital and am of the opinion it should first be discussed and disposed of. If this part of the answer of respondent is supported by the evidence and the law, a ruling to this effect would end the case and no further argument would be necessary. The Trustee concedes and the District Court and United States Court of Appeals found The Hillsboro National Bank and the seventeen other reclamation claimants are entitled to share only as general creditors. This issue is raised by paragraph 4 of the answer of the Trustee (R. 11). That paragraph of the answer is as follows: (4) He (the Trustee) says "that the sale and transfer of the personal property of Litchfield Precision Products to The Gill-Owen Company, a corporation, the present bankrupt, was not such a transaction as required compliance with the Illinois Bulk Sales Law." After discussing this issue, I will discuss the other issues as nearly as possible as they appear in the brief and argument of petitioner. Although this question was directly raised by

the answer filed with the Referee, much evidence heard pertaining to the same presented and argued in printed and oral argument, the Referee in his order filed (R. 120) did not pass on or rule on that question or in any way refer to the same. When an appeal was taken from the order of the Referee to the District Court the same question was presented in the Trustee's Petition for Review of the Referee's Order, paragraph IV, page 124 of the record. The District Court in its Memorandum on hearing on Certificate of Review placed the decision upon the basis that the petitioner, The Hillsboro National Bank, could not prevail as a preferred claimant for the reason that "The bank accepted the benefits of the transfer knowing all the facts, and later when bankruptcy intervened, filed their claim against the corporation as a general creditor" (R. 126, 2nd par.). The District Court did, however, say in the same paragraph: "Under such circumstances, I think it extremely doubtful whether the Bulk Sales Act applies."

As to the application of the Illinois Bulk Sales Law to the questions here involved, I, of course, admit there is such a law. It has been held constitutional and is valid and binding in cases to which it applies. I say that it does not apply to the reclamation claims here involved. The Illinois Bulk Sales Law is in derogation of the common law and must be strictly construed.

24 Am. Jur. Sec. 240, p. 352.

I contend that the transaction here involved, being the change from the partnership to the corporation, does not fall within the provisions of the Bulk Sales Law. It was said in 24 Am. Jur. Sec. 255, p. 360 that the Bulk Sales Act does not apply to the transfer of an entire business to a corporation which has been organized for the purpose of taking over and conducting the enterprise. This is what was done here. The same authority at page 361 said that

the weight of authority has held that such statutes do not contemplate sales of articles which have been kept wholly or partially for use in and about a building wherein business is conducted and that the Bulk Sales Acts have frequently been held not to apply to sales of fixtures, furniture and chattels which are made use of in conducting a business. A direct decision on this question is found in *McLean* v. *Miller Robinson Co.*, 55 F. 2d 232. This decision was based on the Pennsylvania Bulk Sales Act, which is the same as the present Illinois Bulk Sales Law. After holding that the statute is in derogation of the common law and must be strictly construed, the court held that a corporation formed by individuals who transferred all the assets of the business, a partnership, to the corporation was not a purchaser of stock of goods and fixtures within the Bulk Sales Act. The Court there said (p. 233):

> "There is no suggestion of actual fraud. The transaction did not reduce the value of the assets available to creditors, but merely changed their form. Instead of the tangible property, the creditors could proceed against the stock which was indisputably of equal value."

And I might say in the case at bar there was an added sum of $15,000.00, the sale value of the real estate for the protection of the petitioner as the Illinois Bulk Sales Law does not apply to the real estate and the further fact that it could proceed against D. E. Owen, the other partner in the partnership, which is not in bankruptcy.

In the above case in discussing the word "purchase", sale, etc., the Court said:

> "It accords with the general purpose of the act which was to prevent the sudden and secret conversion of the tangible assets of a going business into cash; a medium easily disposed of and difficult to trace or to reach by process. It also accords with the general rule of statutory interpretation that statutes in derogation of the common law must be construed strictly."

Another case in point is *Thorpe, et al.* v. *Pennock Mercantile Co., et al.*, 99 Minn. 22, also reported in American and English Annotated Cases, Volume 9 at page 229. The Court there held that where an insolvent trading corporation, acting in good faith and without intent to defraud, transfers its merchandise and other property to a corporation organized for the purpose of getting new capital into the business, and the partners become stockholders in the corporation, and the corporation, after carrying on the business for a while, becomes insolvent, the creditors of the corporation are entitled to priority over the creditors of the partnership, though the transfer of the property is made without compliance with the provisions of a statute regulating sales of merchandise in bulk and providing that sales made in violation of the statute will be presumed to be fraudulent and void. Many cases are cited in this opinion decisive of the questions here involved. On page 233 of the same volume and opinion, the Court said:

> "It will be noted that the contest in the present case is not between the creditors of the partnership and the creditors of the individual partners. It is between the creditors of the partnership and the creditors of its successor to which the partnership property was transferred. These new creditors may well be regarded as on a higher plane than the creditors of individual partners. In *Francklyn* v. *Sprague, supra*, it is held that a corporation formed by, and consisting of, the members of a partnership for the purpose of conducting the partnership business and taking the partnership property takes the latter free from the partnership equities. Mr. Justice Bradley said: 'The argument that the corporation, being the creature of the partners, was not a bona fide purchaser, and must be considered as having taken the property subject to all partnership equities against it, is not a sound one. The constitution of the corporation and the transfer to it of the property were authorized by law, and were intended to settle and extinguish these

equities and to place the concern on a new footing; and the very parties entitled to equities were the ones who organized the corporation, and made the conveyance to it. Besides, it is not the corporation alone which is concerned in the transfer, but the creditors who trusted it after it was formed. They, or at least the great mass of them, certainly stand in the position of bona fide claimants against its property and assets.' The fact that the partnership was insolvent at the time of the transfer has an important bearing upon the issue of fraud. It is not, however, conclusive, and it does not deprive the parties of the right to show if they are able to do so that the transfer was made for a good and adequate consideration. Nor does it create in itself a lien for the partnership creditors independently of the equity of the partners to have the partnership property properly applied. 1 Bates Partnership, Sec. 560; *Allen* v. *Center Valley Co.*, 21 Conn. 130, 54 Am. Dec. 333; *Case* v. *Beauregard, supra.*

"We are thus brought back to the question whether this transfer to the corporation was made with the intent to defraud the creditors of the partnership. The court has found that the sale and transfer were made in good faith without fraudulent intent, and the evidence is amply sufficient to sutsain this finding."

Another case directly in point and to the same effect is *Maskell* v. *Spokane, etc.*, 100 Wash. 16, cited in L. R. A. 1918C, 929.

The law laid down in the foregoing citation is sufficient to show that there was no actual fraud in the present case and that the requirements of the Illinois Bulk Sales Law did not apply to the reorganization and continuance of this business in the manner shown by the evidence herein. As to the manner in which the sale or transfer or reorganization took place, I refer to the testimony of David E. Owen, who was a member of the Litchfield Precision Products, a partnership, and also an incorporator and owner of a majority of the stock of The Gill-Owen Company, bank-

rupt, shown in his testimony (R. 19). He told the reason for the reorganization and the manner of carrying it out (R. 21-22, 25-26, 28-29). He testified that the transfer was made on August 31, 1948 and that prior to that time the Litchfield Precision Products was heavily indebted. They needed new capital, their creditors were pushing them and the facts show that some judgments had been taken against the partnership. Owen and Mr. Gill consulted with Mr. Kinder, an attorney, and discussed the necessity of giving notices under the Bulk Sales Law. They also discussed the matter with Mr. Fisher of The Hillsboro National Bank, which presents this reclamation claim. He stated that the personal property of the Litchfield Precision Products remained in the same building where some of it was rearranged and that the only change made was that the offices of The Gill-Owen Company that were down towards the other part of the building were moved a little closer down to it in the same building; they retained the same employees and bookkeepers and used up the stock that The Gill-Owen Company had on hand in making new equipment which was sold and applied to the payment of the debts of these reclamation claimants. He and Mr. Gill, the other partner, took stock in The Gill-Owen Company. They were then doing business at The Hillsboro National Bank, were overdrawn at the time and talked to Mr. Fisher, president of The Hillsboro National Bank, at a time which he would not specify, but it was immediately thereafter. Mr. Gill, the other partner, testified to the same effect and the reason and manner of making the transfer to The Gill-Owen Company, saying (R. 98) they moved the office in the same building only a few feet; used the merchandise, stock in trade of The Gill-Owen Company and paid debts of the partnership therefrom (R. 103); and that the Litchfield Precision Products partnership was absorbed into The Gill-Owen Company (R. 109). Juanita Goff, bookkeeper

for the partnership and The Gill-Owen Company, testified that checks issued on Litchfield Precision Products forms were paid from The Gill-Owen Company bank account (R. 51); also the partnership overdrafts were paid by The Gill-Owen Company after it was absorbed by the corporation (R. 51). I, therefore, urge that the transfer was not subject to the Bulk Sales Law but that there was merely a continuation of the same business under the new name, The Gill-Owen Company, for the benefit of the creditors of both organizations.

II.

The Petitioner Having Had Actual Knowledge of the Transfer or Sale of the Personal Property of Litchfield Precision Products and Having Participated in Making the Sale and Received Benefits and Payments Thereunder Is Estopped to Now Claim a Prior and Preferred Lien and Is Also Barred by Ratification, Waiver and Laches and Is Permitted to Share in the Proceeds Only as a General Creditor.

If the transfer was void or voidable for failure to comply with the provisions of the Illinois Bulk Sales Law, then has the petitioner lost its claim to a prior or preferred claim or lien on the personal property by reason of waiver, laches or delay, ratification or estoppel or by accepting payments on its indebtedness or by participating in the bankruptcy proceedings as alleged in the answer of respondent?

I further urge, however, that if the Illinois Bulk Sales Law did apply to this transaction that The Hillsboro National Bank by its acquiescence therein is estopped to now assert any claim for a prior or preferred lien or claim. A creditor can be estopped from relying upon a sale made in violation of the Illinois Bulk Sales Law. No transaction

is so void that its terms cannot be waived or that one who participates therein by receiving its benefits cannot be estopped to assert that he can keep the benefits received and yet repudiate the transaction. A bankruptcy proceeding is in a court of equity and governed by equitable rules and considerations. Here the petitioner and other reclamation claimants in effect say: "We will accept the transfer from the Litchfield Precision Products, the busted partnership; take the additional security of the newly formed Gill-Owen Company with its $24,000.00 of real estate as added security and the personal property; accept payments of several thousand dollars cash from its assets and go along with it for a long period of time, then when its credit and assets slump, come into a court of bankruptcy and say 'I have been defrauded; give me back its assets as a preferred claim,' " to the exclusion of day laborers, federal, local, income and other government taxes, withholding wages and common creditors. This claimant, the petitioner, is not in this court with the "clean hands" as required in a court of equity. The Referee in his certificate and decision said that he found no evidence of waiver or estoppel on the part of The Hillsboro National Bank that would allow any other determination. I do not believe the Referee gave sufficient consideration to the acts and conduct of The Hillsboro National Bank and its officers with regard to the entire transaction, from the date of the transfer, August 31, 1948 to the time it filed its reclamation claim twenty months thereafter, which I urge conclusively and definitely shows the bank to be guilty of laches in asserting its claim and is now estopped to urge that the sale or transfer was made in violation of the Illinois Bulk Sales Law. The Illinois Bulk Sales Law does say that if the sale was made without giving notice to the creditors, the sale as to the creditors is void. It does not say that a creditor could not rely upon the sale if he saw fit to do so as was done in this

case by The Hillsboro National Bank. Many law writers of high repute have discussed the effect of waiver, laches and estoppel by a transaction that otherwise would have been illegal or void. Many courts have also passed on this question. The courts of Illinois have frequently passed on the present Illinois Bulk Sales Law when considering the same questions. I refer to a few of these citations.

Jeffry Hotel Corp. v. *Chicopulos,* 262 Ill. App. 537.

A creditor is estopped to complain that notice was not given under the Bulk Sales Law, if he in fact participated in and took the benefits of a transaction with full knowledge that such notice was not given.

Brady v. *Marshall,* 302 Ill. App. 151.

On page 158 of that opinion, the Court said:

> "it would seem on principle plaintiff would be estopped to complain that notice was not given under the Bulk Sales Act, if he in fact participated in and took the benefits of a transaction with full knowledge that such notice was not given."

In *Aaron* v. *Dausch,* 313 Ill. App. 524, the Court held that creditors could waive their rights. The petitioners had a right under the Bulk Sales Law, if it applied to this type of transaction, to immediately proceed against it to collect their accounts, but they could not wait a year and a half, accept the benefits by receiving large payments and now proceed to set the sale aside under the Bulk Sales Law after the property had passed into the hands of the Trustee in Bankruptcy and yet retain the payments made and benefits received. The petitioner here elected to allow the sale by the partners of Litchfield Precision Products on August 31, 1948 to stand and accept The Gill-Owen Company, a corporation, as further security in addition to the Litchfield Precision Products and accepted payments from it and have taken part in the bankruptcy proceedings. Most of these claimants have presented their claims to the

Referee in Bankruptcy, participated in the selection of a Trustee and therefore are estopped by their action and have thereby ratified the sale.

In *Milwaukee Commercial Bank* v. *Bennett,* 249 Ill. App. 456, the Court discussed the matter of fraud and held that fraud could be waived, and at page 461 said:

> "It is a well settled principle of law that one who finds that he has been defrauded must, after the discovery of the fraud and at the earliest opportunity, ask to have the transaction rescinded and the parties placed in statu quo. *Resser* v. *Corwin,* 72 Ill. App. 625; *Cox* v. *Montgomery,* 36 Ill. 396."

It was held in *C. & E. Marshall Co.* v. *Leon,* 267 Ill. App. 242, that a failure to comply with the terms of the Bulk Sales Law in selling does not render the sale void but voidable only as to creditors. The Court held that a creditor could ratify the sale, he could waive it and is estopped to take any advantage of the failure, if having knowledge of the same the creditor accepted benefits from the new corporation that took over the property or waited an undue length of time to proceed or did anything else that would tend to ratify the act. These matters are all true in the present case with reference to all of the claimants under these reclamation petitions.

The acts of the petitioner as shown by the evidence and its attitude toward the transaction with reference to its claim when considered with the holdings of the courts and text book writers as to the remedies allowed a creditor when a sale has been made without complying with the Bulk Sales Law fully answers the statement in petitioner's brief (p. 19) wherein counsel say "there was nothing petitioner could do to set aside what had already been done." The petitioner could have filed a suit at that time to set aside the sale and have the personal property of the partnership attempted to be transferred or absorbed by the corporation

then promptly applied on the payment of its claim and indebtedness, instead of participating in the transfer and for twenty months accepting the benefits arising to it and the other reclamation claimants wherein the petitioner bank itself received on its indebtedness to the exclusion of other general creditors a sum of more than $20,000.00 and the other reclamation claimants received more than $11,000.00 on their claims in addition to other security given by the transfer. Instead of proceeding promptly to do this, which was their legal right under the laws and decisions of the courts of the State of Illinois it, through its officers and managers and attorneys, refused or failed to move promptly but exerted additional time, effort and energy to have the plant continue its operation and to make payments on their claims for the monies earned by a continued operation of the plant. They went along with the transfer as long as the going was good, then when bankruptcy intervened, took additional notes and mortgages, filed its claim as a general creditor and several months thereafter filed its reclamation claim saying that the transfer made so many months before was void and asked to have ninety per cent of the remaining property turned over to it in addition to the many thousands of dollars paid during the operation of the plant by The Gill-Owen Company after the transfer and prior to the bankruptcy. This is what petitioner could have done and fully answers the statement that there was nothing petitioner could do to set aside what had already been done. The petitioner instead of getting the remaining ninety per cent ought to be required to pay back what it received after the transfer, before it filed its reclamation claim. This would be equity and this would be coming into court with clean hands.

That the Illinois Bulk Sales Law was not void but only voidable is as a proposition of law amply sustained by the various Illinois decisions heretofore referred to and the

decision in the case of *Evans* v. *Herbranson,* an Iowa case reported in 15 A. L. R. (2) 925 and the annotation thereof referred to in the opinion of the United States Court of Appeals which is now so severely criticized by the petitioner. That decision held that a statutory provision that, in the absence of compliance therewith, a sale in bulk shall be "void" as against creditors of the seller, means that the sale shall be voidable. The only question therefore is what extent of participation, acquiescence or delay by the creditor renders the statute voidable and estops the creditor who fails to take immediate steps to protect his right from thereafter asserting that the transfer was void instead of voidable. The many cases cited in the annotation to this decision fully carry out and justify my position that the Illinois Bulk Sales Law as applied to the facts here did not render the transfer void but that it was only voidable and that the petitioner not having promptly acted is now estopped from asking that the sale be declared absolutely void.

As fully shown by the evidence, it appears that The Hillsboro National Bank, by its president, personally appeared at the first meeting of creditors and had full knowledge of the filing of the bank's claims and knew of the appointment of the Trustee and for many months thereafter its claims were on file in the office of the Referee, forming the basis for a general claim along with the other creditors. After the reorganization and transfer of the personal property of the Litchfield Precision Products, the partnership, to The Gill-Owen Company on August 31, 1948, this bank received large payments of money on the indebtedness formerly owed by the Litchfield Precision Products and specifically assumed by resolution on the corporate records of The Gill-Owen Company (R. 48, 85, 89, 117). These payments and benefits this reclamation claimant and the others standing in the same light have kept and applied on the

payment of the indebtedness of the Litchfield Precision Products incurred before the transfer or reorganization, and owing to the reclamation claimants. Each of the items marked "paid" shown in the statement of claims of reclamation petitioners (R. 117) were paid after the transfer of the Litchfield Precision Products to The Gill-Owen Company on August 31, 1948 under the assumption agreement. They aggregate more than $14,000.00. These creditors insist on keeping this money, to the detriment of the common creditors and in addition here claim to have a prior lien upon the proceeds of the sale of the personal property so transferred. Gilbert's Collier on Bankruptcy, Second Edition, page 1220 says:

> "A person should exercise his right of reclamation on the ground of fraud before he has of his own volition placed himself in the position of a creditor, for if he joins in the election of a trustee, with knowledge of the fraud perpetrated against him, he is estopped from thereafter insisting on a return of the goods."

And in this case from insisting upon a lien upon the money arising from the sale of the personal property. This the bank did and by law and its own acts is precluded from asserting its reclamation claim. There is an old maxim, the substance of which is that one who does not speak when he ought to speak, cannot thereafter speak when he wants to speak, or a more common expression brought down to date is that one cannot eat his cake and have it too. So, therefore I insist that this reclamation claim of The Hillsboro National Bank should be disallowed, giving it only the standing of a general creditor along with the other creditors who have not received the benefits of this reorganization and additional security and money payments that was received by The Hillsboro National Bank and the other reclamation claimants. A decision on this claim by the Stipulation will decide the remaining claims standing

in the same category. The allowance of this claim as a prior lien would by many times over wipe out all of the money now in the hands of the Trustee arising from the sale of the personal property of the said corporation.

As shown by the Certificate of Referee for review and his findings therein, it is apparent that the Referee was of opinion that the reclamation claim of The Hillsboro National Bank and the others dependent thereon should have been denied, were it not for the decision *In Re LeMaire Cosmetic Co.*, 174 F. 2d 749, being a decision of the Court of Appeals of the Seventh Circuit rendered on May 16, 1949, now principally relied upon by petitioner. I, with the attorneys for the common creditors and for the government, have fully considered this opinion. While the opinion was no doubt correct upon the facts shown in the case tried, I believe the case is so completely distinguishable from the one at bar that it is not adversely decisive of the questions here involved, but in fact strengthens my contention that these reclamation claims should be denied. In the *LeMaire* case a chattel mortgage had been given upon the personal property that had belonged to an individual and used in his business and thereafter formed into a corporation owned by the same party. The chattel mortgage was executed May 10, 1946. At that time the mortgagee had no knowledge that the business had been changed from individual ownership to the corporation. Galsworthy, the mortgagee, was unaware of the existence of the debtor corporation until on or about the date of the execution of the mortgage and the facts showed it was really not until after the mortgage was executed. There was no change in the bank account; the business had been continued in the name of the individual as a sole owner. There was no fundamental change in the conduct of the business and to all intents and purposes the former owner continued the business, notwithstanding he had organized a corporation

to take it over. There was no bill of sale of the property from the individual to the corporation, hence Galsworthy, the holder of the mortgage, never had any notice or knowledge of the sale of any kind either under the Bulk Sales Law or in any other way and had no knowledge of the relation existing between Martin and the corporation. This formed the basis for the decision of the Court, which said, p. 752 of 174 F. 2d, in which the case is reported:

> "This premise might be relevant to an issue between Martin, the individual, and the corporation, but we think it is of no consequence as between either the corporation or Martin and a third party, such as Galsworthy in the instant matter. Especially is this so where such third party was without notice or knowledge of the relation existing between Martin and the corporation."

Also, on p. 753, the Court said:

> "Moreover, if we assume that the meager and dubious proof discloses a transfer of the property as between Martin and the corporation, we think such transfer could not be binding upon Galsworthy, who was without notice or knowledge."

The Court by use of the language "without notice or knowledge of the relation," etc. certainly implied that if Galsworthy, the holder of the chattel mortgage, had knowledge of the facts, he would have been barred from asserting his claim regardless of whether he had notice under the Bulk Sales Law or not. Apply that statement to the issue made by the claim of petitioner, The Hillsboro National Bank, and the knowledge of the relation existing between the Litchfield Precision Products, the partnership, and The Gill-Owen Company, the corporation, and the decision in the *LeMaire* case would be an authority for disallowing the claim of the petitioner, The Hillsboro National Bank. In the *LeMaire* case, Galsworthy had less than ten days in

which to obtain the information, which was not made public and not divulged to Galsworthy, the mortgagee. In the case at bar, the evidence in the record heretofore referred to showed absolute knowledge by the petitioner in every particular of the financial standing of the Litchfield Precision Products, The Gill-Owen Company, David E. Owen and Edmund A. Gill, the owners and prime movers in all of the varied operations and even before the transfer. Here the bank financed all of the parties; Mr. Fisher, president of the petitioner bank, visited the plant, saw the machinery, inquired as to who their attorneys were that advised the transfer or reorganization; transferred the bank account from the Litchfield Precision Products to The Gill-Owen Company; took a chattel mortgage on the property, also a real estate mortgage, which the bank did not record; paid the payroll of The Gill-Owen Company upon checks of the Litchfield Precision Products as a matter of convenience or economy; indicated on the bank books from what fund the payment was made; took new notes and entered into an agreement by which payments were to be made on the account of the Litchfield Precision Products indebtedness out of funds realized from the operation of the newly-formed The Gill-Owen Company; accepted trade accounts and credited the same on its indebtedness; permitted meetings of the stockholders, creditors and partners of the two concerns to be held in the bank and participated in said meetings with an effort to finance the operation of the same; proceeded in this manner for a period of more than seventeen months after August 31, 1948, the date of the transfer or reorganization about which they now complain and until long after the bankruptcy proceedings had been filed. The bank, through its president, Mr. Fisher, appeared at the first hearing of creditors and participated in the proceedings for the selection of a Trustee and appeared at other hearings, all before he or

the bank saw fit to say that the transfer from the Litchfield Precision Products to The Gill-Owen Company was illegal because they had no notice of the same. Had knowledge of the same kind and effect been shown in the *LeMaire* case, no doubt the holding of the court would have been otherwise.

I, therefore, urge that the Referee in rendering his decision failed to distinguish between the finding in the *Le Maire* case and the findings in other cases in the former part of this brief referred to. The District Court and United States Court of Appeals did so distinguish. The Referee stated that he found no evidence of waiver or estoppel on the part of The Hillsboro National Bank. The District Court and United States Court of Appeals did so find in four different decisions or rulings. If the facts in this case shown by uncontradicted testimony do not establish estoppel, I am wholly at a loss to conceive a state of facts that would in any case amount to an estoppel. Estoppel has been defined by many text book writers and decisions of our courts. The simplest definition is found in Bouvier's Law Dictionary, 12 Ed., Vol. 1, p. 541, in which it is said:

> "ESTOPPEL. The preclusion of a person from asserting a fact, by previous conduct inconsistent therewith, on his own part or the part of those under whom he claims."

That definition deeds no enlargement. If all other questions are put aside in the determination of these claims, the defense urged by the answer filed herein that the petitioner, The Hillsboro National Bank, was estopped to ask for a recovery of the property or to have its claim allowed as a preference, and would be sufficient to justify a denial of the same. Whenever this question has come before the courts of Illinois on a state of facts similar to those here involved the ruling has uniformly been the

same as that applied by the District Court and United States Court of Appeals for the Seventh Circuit, to which the Writ of Certiorari is sought to be directed.

III.

Novation—The Rules of Law as to a Novation Are Not an Issue in This Case.

Counsel for petitioner argue extensively and cite many cases to show that the District Court and the United States Court of Appeals erroneously neglected to apply the rules of novation in deciding the case. That rule is not involved here. The question was not presented or argued by petitioner at the hearing before the Referee. Neither was it argued or referred to in petitioner's brief in the District Court until the case had been fully presented, argued and there decided and not until the motion for a new trial or to set aside the order was filed in the District Court. The District Court did not hold that the contract of The Gill-Owen Company entered into on August 31, 1948 assuming the indebtedness of Litchfield Precision Products and agreeing to pay the same in any wise released the partnership or its partners or its property from its obligation to pay the debt to the plaintiff bank or any other creditor. The decision of that court and that of the United States Court of Appeals merely held that the reclamation petitioners have no right therein superior to that of a general creditor (R. 126, 127, 128). Then again in deciding the motion of petitioner here for a new trial, the Court said (R. 137):

> "The question of petitioner's right to recover from the partnership was not before the court. The court certainly did not hold that petitioner was not entitled to recover from the members of the partnership any sums rightfully due it and which had not

been paid by the corporation. I know of no reason why it should not so recover * * * I did not hold that there had been a novation and do not now so hold." (R. 137.)

The holding of the District Court does not as asserted by counsel for the bank constitute a novation. A plain and simple definition of a "novation" is set forth in Volume 39, American Jurisprudence in paragraph 2, page 255 in which it is said: "A novation, then, as understood in modern law, is generally defined as a mutual agreement among all parties concerned for the discharge of a valid existing obligation by the substitution of a new valid obligation on the part of the debtor or another, or a like agreement for the discharge of a debtor to its creditor by the substitution of a new creditor." And, in the same volume, page 264, it is said: "The effect of a novation by the substitution of a new debtor is to extinguish the liability of the original debtor. For obvious reasons the mere assumption of the debt by the new debtor cannot have this effect." These definitions are so fully supported by the many decisions of our state and federal courts that I do not consider it necessary to burden the Court with the citations. Here, there was no effort to extinguish the original debt of the partnership to the bank or other reclamation claimants. The transaction was done and accepted by the reclamation creditors not to extinguish their claims but to give each of them further security for the payment of the same. This was manifested by the action of the parties in taking notes and receiving payments on the same from the earnings of The Gill-Owen Company, the bankrupt. The amounts paid after the assumption by the corporation were substantial; some of the reclamation claimants receiving as much as eight-tenths of their claim (R. 117) and the petitioner, The Hillsboro National Bank, received many thousands of dollars on its

claim; these transactions extending over a period of nearly two years after the assumption of the indebtedness. Had not bankruptcy intervened, the claims would no doubt have been fully paid by The Gill-Owen Company. The fact that Mr. Fisher testified he retained some of the notes so that he could retain his claim against the partnership adds much strength to the fact that the transaction was merely to give the bank and other creditors further security for their claim and not to extinguish it. Therefore, the extended argument of counsel to show that the order of the court held the assumption to be a novation is entirely without foundation and entirely foreign to any issue here involved.

The Bulk Sales Law was not passed to aid a creditor in perpetrating a fraud. It was passed for the purpose of protecting a bona fide creditor who, without notice and without knowledge of the transaction, was defrauded by a sale. Here the bank was not defrauded. The officers of the bank had full knowledge at all times, if not before the transaction, within a very few hours after the sale took place. They accepted large payments received from The Gill-Owen Company before its bankruptcy from money and material furnished by other general creditors, from the work of employees who have not been paid, to the exclusion of the local government as to taxes, the United States Government as to income taxes and from withholding benefits and Social Security taxes which should have been held for the benefit of those entitled to it. After doing all of this, they now come in and cry "fraud," and ask the court to give them a preferred lien on ninety per cent of the proceeds of the sale, to the exclusion of the others above referred to, who should at least receive their just portion of the same.

In a recent decision of the Supreme Court of the United States (*Nathanson* v. *National Labor Relations Board*,

Advance Reports U. S. Supreme Court Lawyers Ed. U. S. 97 L. Ed. Advance page 13), the court in speaking of priorities generally in a bankruptcy case, held that the theme of the Bankruptcy Act is "equality of distribution." That principle would be here violated if the petitioner and other reclamation claimants are permitted to keep all the payments made on their indebtedness, amounting to many thousand dollars as shown in their statement of claims (R. 117), in addition to receiving the benefit of the stock of material on hand at time of the transfer owned by the partnership and by The Gill-Owen Company, to the exclusion of other creditors, then here get ninety per cent of the balance on hand from the sale of personal property and also get the added security and benefit of the real estate owned by The Gill-Owen Company on their deficit, if any, and share in the balance as a general creditor.

To enter such an order and judgment would be unjust and inequitable and aid the petitioner in perpetrating a fraud on the general creditors.

David E. Owen, who was a partner in Litchfield Precision Products, the partnership, and an incorporator of The Gill-Owen Company, now bankrupt, was a principal witness for petitioner in this case. The evidence shows that he has a similar reclamation claim for $47,000.00 pending, its outcome not to be determined by the decision in this case. The evidence also shows she took away machinery just before or immediately after the transfer to this corporation (R. 70). It also shows that he, Owen, took out of the assets of Litchfield Precision Products $8,500.00 to pay for his stock in The Gill-Owen Company (R. 37). If this court holds that the transfer from the partnership to The Gill-Owen Company was void for failure to give written notice under the Bulk Sales Law and that it cannot be waived nor the reclamation claimants

estopped by reason of actual knowledge of the transfer and participation therein, then any creditor can attack the sale or transfer at any time and in any way directly or collaterally and have a preferred lien on all the personal property of the partnership now held by the bankrupt. That might permit Owen to maintain his claim of $47,000.00. Such a conclusion would be highly inequitable and unfair to all the general creditors and permit the Bulk Sales Law to become a fraud instead of a protection.

Conclusion.

I have not in this brief and argument for respondent discussed or tried to distinguish the many authorities, texts or statutes, more than twenty in number, cited by petitioner, to support its position taken in effort to reverse the judgment of the District Court and United States Court of Appeals. To do so would unduly extend this argument to such length as would be in violation of the rules of this court. Most of these authorities were also cited when the case was in the District Court and United States Court of Appeals and there had consideration. I, as attorney for the Trustee, and other attorneys interested in behalf of the government and some general creditors have read and considered all of them. I say without fear of successful contradiction that none were in cases wherein the facts were the same or even similar to the facts in the case at bar. The authorities cited were no doubt proper decisions upon the facts and legal questions involved in the respective cases. No case or decision of any court is a proper guide in any other case except insofar as the facts and issues involved are the same. When the evidence in this case as shown in the transcript is considered it will show a chain of conduct on the part of the petitioner, its officers and employees, and the part-

ners of Litchfield Precision Products and of the officer directors and stockholders of The Gill-Owen Company, th bankrupt, as to fully convince this court that the peti tioner with full knowledge of the transfer has by acqui escence, estoppel, laches, participation and connivance i the whole transaction, before, at the time of and after th sale, transfer or absorption of the partnership into th now bankrupt corporation, barred itself from maintainin its claim for a preferred lien or claim. I have endeavore to, and believe I have, cited authorities that are in poin upon issues and legal questions similar to the ones herei involved. Some of them from Illinois courts construin the Illinois Bulk Sales Law, which should be followed b this court in applying the Illinois Bulk Sales Law to fact proven in this case.

The judgment and order of the District Court an United States Court of Appeals were correct. They ar supported by all the evidence and are not contrary to an law, statute or decision of any court, State or Federal when applied to and based upon a state of facts as show in this case.

I, therefore, submit this brief and argument in behal of the Trustee who represents the general creditors an urge that the petition for writ of certiorari be denied.

Respectfully submitted,

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